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The City of New York

OFFICE OF THE
COMPTROLLER

ANALYSIS OF THE TRANSIT
COMMISSION'S PLAN FOR RE-
ADJUSTING THE SECURITY
ISSUES OF TRACTION COM-
PANIES AND MAKING NEW
CONTRACTS FOR PRIVATE
OPERATION OF MUNICIPALLY
OWNED LINES

By
CHARLES L. CRAIG
Comptroller

OCTOBER 8, 1921

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THE CITY OF NEW YORK

OFFICE OF THE COMPTROLLER

CHARLES L. CRAIG
Comptroller

On September 29, 1921, the Transit Commission appointed by Governor Miller announced a "Plan of Readjustment of New York City Street Railroads." What the plan involves is shown in detail in the analysis that follows this

SUMMARY OF WHAT THE TRANSIT COMMISSION'S PLAN PROVIDES

1. Release of the Interborough and the Brooklyn Rapid Transit corporations from their contract obligations to operate the dual subway system at a five-cent fare for forty-nine years.
2. Release of the New York Railways and other surface lines from franchise obligations for a five-cent fare.
3. Release of all lines from all obligations to pay franchise taxes or any other kind of taxes.
4. The surrender by the City of its lien upon all of the equipment provided by the Interborough under contracts Numbers 1 and 2, given as security for faithful performance by the Interborough of its contract obligations and which may be foreclosed as a mortgage upon default.
5. Release of the Interborough from the obligation of \$1,000,000 continuing bond for the performance of its contract obligations.
6. Release of the B. R. T. from the obligation of \$1,000,000 continuing bond for the performance of its contract obligations.
7. A cost plus fare to be fixed from year to year by a Board of Control composed of one representative from the Interborough, one from the Brooklyn Rapid Transit, one from the surface lines, three to be appointed by a Mayor hereafter to be elected, and the seventh to be acceptable to the traction representatives or appointed by the Transit Commission. This is a body packed from the start with traction men.

8. The death-knell of Municipal operation for at least two generations to come.

9. The buses so persistently refused to the City by the Miller Legislature are to be given to the street railway interests.

10. The lines that have failed in private operation are to be unloaded on the City at a valuation acceptable to their security holders, and bonds guaranteed by the City's investment in its subways to earn five per cent., and which may earn as high as six and one-half per cent., are to be delivered in exchange for securities now outstanding, many of which are unsalable and some of which are quoted at less than five cents on the dollar.

11. Speculation in bonds instead of stocks, with an insider's device for market manipulation unsurpassed by any ever used for plundering a confiding public.

12. The brutality and public-be-damned service that has characterized the private operation of privately owned traction lines in New York City during sixty years of jobbery and exploitation by crooked financiers is to be relicensed and confirmed in the possession and operation of the City's own lines for two generations to come.

13. Upon the release of the Interborough and the Brooklyn Rapid Transit from their present contracts for a five-cent fare and the purchase by The City of New York of all the elevated and surface lines now privately owned and operated, all of such lines and the City's subways are to be turned over to the Interborough, the Brooklyn Rapid Transit and the surface lines (under new names) for private operation, guaranteed against loss, for two generations to come. In other words, all of the vices, scandals, degradations and oppressions from which the people of New York City have suffered for sixty years at the hands of unscrupulous railway operators count for nothing in experience, and the properties owned and acquired by the City with the public's money are to be left to the exploitation of those whose sole interest is the toll which they can exact from a helpless and betrayed populace.

14. The Interborough under a new name gets back for operation at an increased fare and no taxes the very same lines it now operates at a five-cent fare.

15. The Brooklyn Rapid Transit under a new name gets back for operation at an increased fare and no taxes the lines heretofore in the Brooklyn Rapid Transit system and operated at a five-cent fare.

16. The surface lines of the New York Railways and others now operated under a franchise obligation for a five-cent fare, are to be operated by a company with a new name at an increased fare.

17. When the Transit Commission says that the Manhattan Elevated and the New York Railways and other lines, now privately owned—

“are to be acquired *without cost to the city* by amortizing out of earnings the valuation fixed by the Transit Commission,”

it means that fares are to be increased and out of the increase the present security holders are to receive a price acceptable to them and guaranteed by a purchase money mortgage under which they can take back their lines whenever through mismanagement or default the private operators of the City's lines fail to meet their obligations. It is anticipated that they will fail to meet their obligations, otherwise a purchase money mortgage would be unnecessary.

18. The revenues from the City's own properties amounting to upwards of \$150,000,000 a year are to be collected and handled by a Board of Control, a majority of whom are the direct representatives of the Interborough, the Brooklyn Rapid Transit and surface railways, and one other to be agreed to by them.

19. The domination of the City's properties for two generations to come by an absolutely irresponsible Board of Control against which neither The City of New York, nor any of the people therein, have any redress whatever.

20. The water that has been squeezed out of the mass of traction securities sold to the public is to be put in again. The price to be paid by the City is guaranteed five per cent. bonds for outstanding traction stocks and bonds is to be determined, not by what they will bring in the open market, but by

“a new valuation which will represent the real values in the transportation properties”

according to the statement of Mr. McAneny and his associates.

ANALYSIS OF TRANSIT COMMISSION'S PLAN

Reckless and Irresponsible Statements Concerning the City's Debt Limit Calculated to Damage Its Credit and Help the Traction Interests

Discussion of the Transit Commission's "plan of readjustment" and the statement of Mr. McAneny and his associates in regard to it, require at the outset that attention be called to the irresponsible character of the public utterances of the Transit Commission. On October 4th Mr. McAneny in a public statement asserted that the City's debt margin of \$137,000,000 should have huge deductions made from it, among which he specified \$57,000,000 for a school program and \$30,000,000 for departmental improvements. By this process he announced the conclusion that the debt margin is really only about \$10,000,000, which he characterized as dangerous.

Mr. McAneny's assertion in regard to the public school requirements overlooks that \$41,128,000 has already been charged off against the debt limit in arriving at the net amount of \$137,000,000. His assertion in regard to \$30,000,000 expenditures for departmental improvements is in flat disregard of the pay-as-you-go act, which prohibits the use of the City's debt margin for any such purpose.

The stamp of irresponsibility that attaches to such public utterances of Mr. McAneny must necessarily also attach to any assertions that he or his associates may make in regard to the transit situation, for a statement calculated to deceive the public to the extent of \$71,128,000 is in the highest degree misleading and irresponsible.

The constant effort on the part of the traction interests and their friends to attack the debt margin of The City of New York is intended to create the public impression that there is an imperative necessity for private operation of the City's transit facilities because, it is alleged, that the City has insufficient credit to get along without the private operators. This explains the violent and unfounded attack of ex-Senator Elon R. Brown, counsel to the Meyer Committee, upon the City's debt margin and his attempt to impair the City's credit. *Mr. Brown, Mr. McAneny and others who attack the City's debt margin and credit in this manner merely express the sentiment of the traction interests and aid the propaganda for private domination of the City's transit facilities.*

The City's debt margin of \$137,000,000 is absolutely puncture proof.

Attempt to Release the Interborough and B. R. T. from Their Present Contracts for a Five-cent Fare in Order to make New Contracts More Favorable to Them

The primary and ill-concealed purpose of the Transit Commission's plan is to release the Interborough and the Brooklyn Rapid Transit from their contract obligations to operate the dual subway system for forty-nine years at a five-cent fare. This is the first and essential step in order to open the way for the "service at cost" or "cost plus" fare; for the companies must be released from their present contracts before they can charge more than a five-cent fare.

The "cost plus" fare is to be provided under new contracts according to which the Interborough and the Brooklyn Rapid Transit, each under a new or reorganized name, would operate the identical properties covered by their present contracts, respectively.

No public purpose can be served by a new contract with these interests. Both the Interborough and the Brooklyn Rapid Transit are now in default in rendering the character of service to which the City is entitled under the dual subway contracts.

"The companies are not giving the character of service their franchises and contracts with the City require them to give."
(Transit Commission report, page 4.)

The Greater New York Charter prohibits The City of New York from entering into a contract with a defaulter. The reason for this is that default is conclusive evidence of irresponsibility, and it is contrary to public policy for The City of New York to make contracts with irresponsible parties. For the City to do so would be "heads I win, tails you lose" for the contractors.

The existing contracts with the Interborough and the Brooklyn Rapid Transit contain provisions intended to insure to the City the full performance of their obligations by the Interborough and the Brooklyn Rapid Transit. The City holds a continuing bond from the Interborough for \$500,000 for the faithful performance of Contract No. 1. It holds a further bond for \$1,000,000 for the Interborough's faithful performance of Contract No. 2, and an additional bond for Contract No. 3. It holds a continuing bond for \$1,000,000 for the faithful performance by the Brooklyn Rapid Transit of Contract No. 4.

In addition to this the City, under Contract No. 1, has a lien in the nature of a mortgage upon all of the equipment furnished by the Interborough for that contract. The contract contains provisions authorizing

the City to foreclose the lien whenever the Interborough is in default, and the City is further authorized upon the default of the Interborough to take over the operation of the lines at the Interborough's expense and for its account, or to employ another operator, or to recapture under Contract No. 3 the recent additions to the Interborough system; while under Contract No. 1 all of the lines of the old Interborough system may be taken by dispossessing the Interborough upon its default.

Somewhat similar provisions are contained in the Brooklyn Rapid Transit contract. *These provisions are for the protection of the City, and the very suggestion that the companies should be released from them is almost criminal.*

None but an irresponsible commission created by the legislature in defiance of the City's rights would have the temerity to suggest that obligations of \$2,500,000 and a mortgage lien of upwards of \$25,000,000 should be canceled and thrown away by The City of New York. It is to be noted, moreover, that the Transit Commission proposes to disregard the provision contained in Contracts Nos. 3 and 4 that they cannot be changed except with the approval of the Board of Estimate and Apportionment.

It is obvious that if the City were to make new contracts with the Interborough, the Brooklyn Rapid Transit and the surface lines, they would afford no protection whatever to the public, for by the precedent now proposed to be established they could be disregarded at the pleasure of the companies without any redress to the City.

Tax Exempt Device a Fraud Upon the Public

By the device of vesting in The City of New York the title to the surface and elevated lines now privately owned, *the properties become tax exempt. This is the object sought by the proposal for the City to acquire these lines.* The companies are not to be deprived of the benefits of operating the lines by change of ownership for they are to receive a new lease or agreement for private operations by them for two generations to come.

This is plain fraud upon the public. The effect of it may be illustrated by a simple transaction. Any house owner could profitably give the title to his property to a stranger, provided the stranger would give him a lease to occupy it for his life at a nominal rental, with authority to will it as he pleases upon his death. All of the burdens of ownership such as the payment of taxes and assessments and repairs, are thus cast upon the new owner, while the benefits of use and occupation remain with the tenant.

Board of Control Packed With Traction Men Clothed With Power to Rig the Market and Plunder Investors

Under the new agreements proposed by the Transit Commission the fare is to be fixed on a "cost plus" basis by a "Board of Control" consisting of seven members, one appointed by the Interborough, one by the Brooklyn Rapid Transit, and one by the surface lines; three by the Mayor hereafter to be elected, and the seventh with the consent of the traction members, or by the Transit Commission. *The Board of Control is packed with traction men from the start.* It appears not to be responsible or accountable to any public authority. In connection with the scheme for a cost plus fare is a device for market manipulation unsurpassed by any other used for plundering a confiding public.

Under the innocent and euphonious description of an "Incentive for Efficient Service," the Board of Control is authorized when the earnings produce more than is necessary for current expenses and to pay the five per cent. guaranteed upon the bonds to be issued in exchange for the now outstanding traction securities, to divide a part of the surplus revenues so as to allow the bondholders an additional 1½ per cent. per year on their bonds, or 6½ per cent. instead of 5 per cent.

In plain English, this means that the inside Board of Control can always determine in advance whether the bonds are to receive only 5 per cent. or the increased return. When they conclude among themselves that for the next year's operation the cars shall be jammed with strap-hangers and all kinds of economies practised in the service, they know in advance that they will accumulate a surplus out of which to pay 1½ per cent. additional on the bonds. *This is the period when the insiders go into the stock market and purchase bonds from the uninformed holders.*

When the year's developments have disclosed that the bonds are to receive a return thirty per cent. greater than the guarantee, it is quite manifest that the market price will advance. *On such an advance the insiders are in a position to sell the bonds purchased at materially lower figures and reap a handsome profit.* They can do more than this. They can go "short" of the market of as many bonds as the public will absorb.

They can then experience an entire change of heart toward the traveling public, and, instead of packing the cars with strap-hangers, with infrequent service in non-rush hours, they will afford as nearly as possible a seat for every fare, with the necessary result that the year's operations will show a serious impairment in the net earnings.

When the results of the operation become known in the stock market the insiders who were short of the bonds at the higher prices determined upon a 6½ per cent. return will unquestionably be able to repurchase them at substantial declines to conform to the 5 per cent. guaranteed return. The only limit to the milking of the market by this device is the memory of the investing public. The operation can be repeated on as large a scale and as often as a confiding public will permit.

Stock market exploitation is the only and continuing reason for private operation of transportation facilities in New York City. The record of the past has been a record of market rigging, and the "Incentive for Efficient Operation" guarantees it for the future. To say that stock speculation is brought to an end because the new form of security is to be bonds merely adds a tinge of respectability to the plundering of the public.

Reference need but be made to the orgy of speculation in the Interborough-Metropolitan 4½'s to see what can happen in bond gambling as distinguished from stock speculation.

Way Opened for Enormous Private Graft

Under the cost plus operation the private operating companies will have control of the purchase of all material and supplies, the fixing of all salaries, fees and commissions and other compensation, and the rental of any private property required. This opens a vista for private graft upon a huge scale. There is nothing to prevent the insiders and the operating companies from organizing equipment and supply companies from which they shall make all their purchases of fuel, supplies and materials of all kinds.

The revenues received from the city-owned properties amounting to from \$150,000,000 to \$200,000,000 per year will be collected, handled and disbursed by the traction packed Board of Control. This irresponsible control of public money invites financial scandals of the first magnitude.

Vices and Indecencies of Private Operation Confirmed for Two Generations to Come

The Transit Commission's scheme, if adopted, would be the death-knell of Municipal operation for at least two generations to come.

The last vestige of justification for private operation disappears with the default and breakdown of the Interborough, the Brooklyn Rapid Transit and the New York Railways and surface companies. When

transportation lines are owned by the City of New York and there is no contract obligation for a fixed rate of fare, there is no justification whatever for granting the concession of operation to private interests. The Rapid Transit Act provides for operation on a cost basis. But this is a provision for Municipal operation and not private operation. The fares are to be fixed with the approval of the Board of Estimate and Apportionment. (Section 30.)

The public has been sufficiently exploited by private operators. The proposal to continue private operation of municipally owned lines is indefensible. It is a license for the brutal and public-be-damned service that has characterized the operation of traction lines in New York City during sixty years of jobbery and exploitation by crooked financiers. Moreover, the Transit Commission's scheme reveals that the buses that the Legislature has so persistently refused to permit The City of New York to operate because of the opposition of the traction interests, are to be turned over to the newly constituted surface lines for private operation and exploitation.

Guaranteed 5% Bonds to Be Exchanged by the City for Depreciated Traction Securities at Values to Be Determined by Their Holders

The surface and elevated lines that have failed in private ownership are to be unloaded on The City of New York at a valuation acceptable to the holders of their securities who are to receive bonds guaranteed to return 5 per cent., and which may be increased to 6½ per cent.

The Transit Commission proposes to fix a valuation on the properties so to be acquired that—

"will represent the real values in the transportation properties."

But in practice the value of the properties will be fixed by the security holders.

While the Legislature attempted to give the Transit Commission authority to compel The City of New York to comply with its determinations, *no such attempt was made in the case of the traction corporations.* Any corporation can accept or reject the valuation or plan of the Transit Commission and the Commission cannot exercise any compulsion in the matter. *The effect of this is, that while the valuation will be proposed by the Transit Commission it will be fixed by the holders of securities well organized in groups and committees of skilful financiers.* For the sum thus fixed as the "real values" guaranteed 5 per cent. bonds secured by a purchase money mortgage and backed by the City's subway investment are to be delivered to the holders of traction securities.

The purchase money mortgage provision is a confession that no confidence can be placed in private operation and that default in the obligation on the bonds will necessitate the foreclosure of the purchase money mortgage and the return of the properties to their present owners.

End of Five-Cent Fare. Heavy Increase Required to Pay Guarantees on Inflation in Bond Issues

The moneys required to pay the interest on these guaranteed bonds and to make up for the loss of taxes by exempting the traction property from taxation will be taken from the farepayers in the form of an increased fare. The assertion of the Transit Commission that for the first year the fare "shall remain at five cents" is intended to chloroform the public while the contract obligation of the Interborough and the Brooklyn Rapid Transit to operate at a five-cent fare for 49 years is cancelled. Deferring the increased fare for one year merely enlarges the increase when it takes effect.

The hope held out that the lines can be operated at a five-cent fare under the Transit Commission's scheme will not be realized for half a century, if ever. How great will be the increase cannot be determined until after the fatal step is taken.

In public discussion of this subject, Mr. Quackenbush, the spokesman for the Interborough, has asserted that the rate of fare must be doubled. In other words, he is for a ten-cent fare.

Mr. McAneny, just prior to his appointment as Chairman of the Transit Commission, at a public discussion before the Brooklyn Chamber of Commerce, expressed faintly the hope that the increased fare would not exceed seven cents.

These two figures may be taken to represent the extremes of the insiders' view. If they are averaged at eight cents it will not be much out of the way. Moreover, the indication of an eight-cent fare is confirmed by the figures of the Transit Commission in connection with the valuation that must be placed upon the privately-owned property proposed to be acquired by the City. It has already been pointed out that the figures and the assertion of the Transit Commission, and Chairman McAneny in particular, must be taken with considerable discount and allowance.

It may be assumed that in its report the Transit Commission has presented the figures in the most alluring manner possible and that in actual practice its assumptions and calculations will turn out to be as far from the facts as were the calculations made at the time the dual subway contracts were entered into by the City.

According to the Transit Commission's report—"without allowance for profits of any nature"—the present annual deficits of the traction companies amounts to \$41,000,000 (page 18). These figures probably do not include additions that will have to be made to provide for any refunding of the large note issues of the Interborough and the Brooklyn Rapid Transit now outstanding.

The Transit Commission's report states that:

"The companies are not giving the character of service their franchises and contracts with the City require them to give" (page 4).

The cost of providing decent and adequate service under private operation, to say nothing of profits, will surely increase the annual deficit at least \$14,000,000, or make it a total of \$55,000,000. When provision is made for interest and amortization upon the new issues of guaranteed bonds required to be issued to extinguish private ownership an addition of at least \$10,000,000 a year will have to be made to the annual charges. This makes the total amount that will have to be provided by an increased fare at least \$65,000,000 per year. It is a safe assumption that allowing for errors and omissions in the Transit Commission's calculations that the annual increase that will be placed upon the farepayers will be nearer \$75,000,000 than any figure furnished by the Transit Commission. The calculations of the Transit Commission are based upon a wild guess as to the amount of bonds that will have to be issued to acquire the lines now privately owned. An increase in the fare of one cent will at most produce \$25,000,000 per year.

To take care of the additional obligations which the Transit Commission's plan contemplates will require nearly, if not quite, three times this sum; or, in other words, an eight-cent fare. This is corroborated by the Interborough's contention of Mr. Quackenbush for a ten-cent fare and Mr. McAneny's declaration before the Brooklyn Chamber of Commerce that he hoped to see the fare kept as low as seven cents.

The assertion of the Transit Commission that in "readjusting securities on the basis of honest value" all the water will be squeezed out is contrary to the fact. *The water is now out. The Transit Commission's plan will let it in again.*

Interborough Consolidated, common, is quoted at 1¼, while the preferred is quoted at 5½ cents on the dollar; Interborough-Metropolitan 4½s are quoted at 13 cents on the dollar; Brooklyn Rapid Transit stock is quoted at 7 cents on the dollar, while the 7 per cent. bonds are quoted at 57 cents on the dollar; Third Avenue stock is quoted at 15 cents on the dollar and its 5 per cent. bonds at 38 cents on the dollar, and Second

Avenue is not quoted and is unsalable. The Transit Commission's plan will let the water flow back into these securities from which it has been squeezed, and a speculative value will result from their inflation for which the public will have to pay.

Subway Profits Go to Pay Elevated Guarantees

It appears from the report of the Transit Commission that the Interborough, in the operation of the City's subways by it for the year ending June 30, 1920, showed an operating profit of \$2,630,953, which was utilized by it to pay its guarantee under the Manhattan Elevated lease, of 7 per cent. dividends on Manhattan Elevated stock and the interest on outstanding bonds.

Idle Talk of a "Constructive" Plan

Critics and uninformed writers are constantly asserting that the Board of Estimate and Apportionment could have cleared up the traction situation and that it has no constructive plan. This has no foundation in fact. *The Legislature has stripped the Board of Estimate and Apportionment of any power except to consent to the exactions of the traction companies. The authority that belongs properly in the Board of Estimate and Apportionment has been taken from it by the Legislature and scattered in other boards and bodies such as the Transit Commission.*

The right to operate buses for the relief of the public has been denied to the City by the Legislature. It now turns out that the buses refused to the City are to be operated by the street railway companies.

As to a constructive plan, it is sufficient to say that The City of New York, *after extended public discussion and mature deliberation*, has entered into elaborate contracts with the Interborough and the Brooklyn Rapid Transit for the construction and operation of municipally-owned rapid transit lines. *These contracts contain provisions designed to protect the City against the default and non-performance of their obligations by the Interborough and the Brooklyn Rapid Transit. To say that such contracts should be treated as a scrap of paper or be cast aside is an affront to an honest public opinion.*

To assume that any kind of a contract can be made with the Interborough or the Brooklyn Rapid Transit, or the surface railways, that they will respect or live up to any better than they have with present contracts and franchises, is absurd. In fact, to let these companies go scot free of their obligations under their present contracts under which they are clearly in default and to make new contracts with them, *puts a premium upon bad faith and dishonesty* in the performance of public

contracts. If the Interborough and the Brooklyn Rapid Transit are unwilling to perform their contract obligations, they should abandon their contracts before they subject their security holders to a greater loss than now confronts them. If the surface railways are unwilling to conform to their franchise obligations they should surrender their franchises as a matter of ordinary decency and in good faith. Until these things are done it is idle to talk about a constructive plan, *meaning thereby one dictated by the traction interests and acquiesced in by supine public authority.*

The flagrant disregard of their contract and franchise obligations by the rapid transit and surface railway companies and their indecent defiance of public opinion, afford no basis for new contracts to be made with them by The City of New York.

CHARLES L. CRAIG,
Comptroller.

October 8, 1921.



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